Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
High-Cost Universal Service Support	)	WC Docket No. 05-337
Federal-State Joint Board on Universal Service	)	CC Docket No. 96-45
Lifeline and Link Up	)	WC Docket No. 03-109
Universal Service Contribution Methodology	)	WC Docket No. 06-122
Numbering Resource Optimization	)	CC Docket No. 99-200
Implementation of the Local Competition Provisions in the Telecommunications Act of 1996	)	CC Docket No. 96-98
Developing a Unified Intercarrier Compensation Regime	)	CC Docket No. 01-92
Intercarrier Compensation for ISP-Bound Traffic	)	CC Docket No. 99-68
IP-Enabled Services	)	WC Docket No. 04-36
Establishing Just and Reasonable Rates for Local Exchange Carriers	)	WC Docket No. 7-135

JOINT COMMENTS OF CITYNET, LLC, GRANITE TELECOMMUNICATIONS, INC., PAETEC COMMUNICATIONS, INC., RCN TELECOM SERVICES, INC. AND U.S. TELEPACIFIC CORP.

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Summary

Citynet, LLC, Granite Telecommunications, Inc., PAETEC, including PAETEC Communications, Inc., US LEC and McLeodUSA Telecommunications, Inc., (hereinafter jointly referred to as PAETEC), RCN Telecom Services, Inc. and U.S. TelePacific Corp. (the "Joint Commenters") submit their recommendations on intercarrier compensation and universal service reforms. Although the Commission should be commended for its efforts, many of the proposals run the risk of being vacated upon appeal and/or could have significant unintended consequences in practice. Thus, as described in the comments that follow, the Joint Commenters urge the Commission to modify its proposed reforms.

INTERCARRIER COMPENSATION REFORM

- **Legal Authority:** Section 251(g) neither supersedes Section 2(b) nor grants the Commission authority to set intrastate rates. Even if the Commission were to overcome these jurisdictional barriers, the intrastate access charge transition proposals are arbitrary, capricious, and inconsistent with Section 252(d)(2). *The Commission should therefore avoid intrastate rate-making.*

- **Transition Period and New Rates:** In the event that the Commission finds authority to mandate interim or permanent intrastate rate reductions, *any transition plan should include a standstill of at least two years, and the states should set the "glide path" to move intrastate access charges to interstate access rates and ultimately Section 251(b)(5) rates*. Given current economic circumstances, the fact that most carriers cannot immediately recover lost access revenues from other sources such as end user retail rates, and the fact that Section 252(d) precludes the Commission from setting even interim rates, a two-year transition to interstate rates is arbitrary and capricious and ultra vires. Moreover, because service-related, geographic, and operational differences exist among service providers, *any methodology should direct states to set rates on a company-by-company basis rather than statewide*.

- **Confirming Interconnection Rights:** *Physical* interconnection is inextricably intertwined with *financial* concerns. The proposals would upset existing interconnection arrangements and substantially increase competitive carrier costs. *The "edge" proposals are therefore inconsistent with the Act and an unexplained reversal of long-standing interconnection policies.* Similarly, if it declares (as proposed) that certain Internet Protocol ("IP")-originated or -terminated services are "information services," *the Commission should reaffirm that all local exchange carriers who serve information service providers* *or self-provide information services have interconnection rights and obligations under Sections 251 and 252 of the Act.*

- **"Additional Costs" Standard:** The record shows that a competitive local exchange carrier ("CLEC") will often have costs many times higher than the presumed result of the new cost standard ($0.0007). Any requirement that CLECs provide termination services without adequate compensation violates the Act and will not survive appeal. *The Commission should reject the new standard or, in the alternative, clarify that it will apply only to IP-to-IP interconnection under Sections 251 and 252. The Commission should also remove specific network design directives and threats to usurp state authority.*

- **"Change in Law" Contract Clauses:** *The Commission should clarify that any adopted reforms constitute a "change of law" for all contracts and preempt state law that precludes carriers from making contract modifications.*

UNIVERSAL SERVICE REFORM

- **Contribution Methodology:** Imposing three different reporting mechanisms on carriers (numbers, connections, and revenues) would be overly burdensome and exacerbate the complexity of the current system. The hybrid numbers/connection system in Proposal B (and the drastic rate increase that would result) would be catastrophic for small businesses and unlawful. *The Commission should streamline and simplify contributions for all federal funds, ensure that any new methodology does not impose double-assessments on consumers or discriminate against providers of stand-alone services, and provide a minimum of one year to transition to any new methodology.*

- **Other Issues Raised in the Further Notice of Proposed Rulemaking:**

    - Originating Access Charges: The Commission has no authority to prohibit originating *intrastate* access charges. Elimination of originating access charges generally (intrastate *and* interstate) would be inconsistent with the Calling Party Network Pays regime that otherwise governs intercarrier compensation, even if reformed as proposed. Finally, eliminating originating access charges at the same time terminating access charges are reduced would impose a substantial burden. *Even if it had authority to eliminate all originating access charges, the Commission should defer any such action until after terminating charges have been reduced.*

    - Traffic Stimulation and Revenue Sharing: The Commission should target any new rules to thwart abusive schemes that drastically increase terminating access traffic to take advantage of high access rates. In particular, *there is general consensus that any rules to address traffic stimulation by CLECs should apply only to those carriers that elect the rural exemption or benchmark to rural rates*. "Revenue sharing" is a long-standing and legitimate business practice that should not be the basis of any traffic stimulation restrictions.

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JOINT COMMENTS OF CITYNET, LLC, GRANITE TELECOMMUNICATIONS, INC., PAETEC COMMUNICATIONS, INC., RCN TELECOM SERVICES, INC. AND U.S. TELEPACIFIC CORP.

I. INTRODUCTION AND BACKGROUND

Citynet, LLC, Granite Telecommunications, Inc., PAETEC, including PAETEC Communications, Inc., US LEC, and McLeodUSA Telecommunications Services, Inc. (jointly referred to herein as "PAETEC"), RCN Telecom Services, Inc. and U.S. TelePacific Corp. (collectively, the "Joint Commenters"), through undersigned counsel, submit their Comments on the *Order and Further Notice of Proposed Rulemaking*.[1] The *FNPRM* has three Appendices, each containing separate proposals, referred to herein as Proposal A, Proposal B, and Proposal C.

The Federal Communications Commission's ("Commission's" or "FCC's") efforts to resolve long-standing carrier compensation and universal service questions are commendable. However, many of the proposals in the *FNPRM* run the risk of being vacated upon appeal, or could otherwise have significant unintended consequences in practice. Finally, in this global environment of significant economic downturn, the timing of radically changing the intercarrier compensation scheme and universal service reform that would foist significantly more cost recovery onto business end users could not be worse. Thus, the Joint Commenters respectfully urge the Commission to modify its proposed reforms.

II. REFORM OF INTERCARRIER COMPENSATION (V.)[2]

A. Legal Authority (V.B.3.)

1. Section 251(g) Provides No Basis for the Commission to Bring Intrastate Access Traffic within the Scope of a Unified Intercarrier Compensation Framework.

Consistent with Section 2(b) of the Act[3] and the jurisdictional fence confirmed by the U.S. Supreme Court in *Louisiana v. PSC*,[4] regulation of intrastate access services and rates has been reserved for the state commissions. In the Proposals, however, the Commission blurs these

[1] *High-Cost Universal Service Support, Federal-State Joint Board on Universal Service, Lifeline and Link Up, Universal Service Contribution Methodology, Numbering Resource Optimization, Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, Developing a Unified Intercarrier Compensation Regime, Intercarrier Compensation for ISP-Bound Traffic, IP-Enabled Services*, Order on Remand and Report and Order and Further Notice of Proposed Rulemaking, Docket Nos. 05-337, 96-45, 03-109, 06-122, 99-200, 96-98, 01-92, 99-68 & 04-36, FCC 08-262 (rel. Nov. 5, 2008) ("*Order and FNPRM*").

[2] The Roman numerals at the end of the section headings correspond to the heading numbers used in Proposals A and C.

[3] 47 U.S.C. § 152(b).

[4] 476 U.S. 355 (1986).

boundaries and mandates adoption of a unified rate for *all* interstate and intrastate traffic by each state commission.

The Commission's effort to bring intrastate access traffic within the scope of Section 251(b)(5) relies in part upon Section 251(g) of the Act.[5] The Proposals state that "… traffic encompassed by section 251(g) is excluded from section 251(b)(5) except to the extent that the Commission acts to bring that traffic within its scope."[6] They then assert that because section 251(g) is just "a transitional device," the Commission has the authority to abolish the existing access regime that has been preserved by Section 251(g), and to place "all traffic under the umbrella of one compensation scheme."[7]

Although the Proposals assume that Section 251(g) preserved *all* pre-existing access regimes (interstate and intrastate) following passage of the 1996 Act, closer review indicates that in fact *intrastate* access traffic was never "encompassed by section 251(g)." To the contrary, Section 251(g) merely preserves pre-1996 Act equal access, compensation, and interconnection restrictions and obligations arising from a "*court order, consent decree, or regulation, order, or policy of the Commission*." Section 251(g) thus does not apply to rules or orders promulgated by *state commissions* to govern *intrastate* rates and services. The Commission itself has acknowledged that Section 251(g) does not extend to intrastate access regimes.[8] Furthermore, the U.S. Supreme Court has made clear that Section 251(g) preserves pre-existing regulatory structures

[5] 47 U.S.C. § 251(g).

[6] Proposal A, ¶ 220; Proposal C, ¶215.

[7] Proposal A, ¶¶ 220-221; Proposal C, ¶¶ 215-216 (both quoting *WorldCom v. FCC*, 288 F.3d 429, 430 (D.C. Cir. 2002)).

[8] *Implementation of the Local Competition Provisions in the Telecommunications Act of 1996; Intercarrier Compensation for ISP-Bound Traffic*, Order on Remand and Report and Order, 16 FCC Rcd 9151, 9168, n.66 (2001) ("ISP Remand Order") (finding that Section 251(g) "preserves only the Commission's traditional policies and authority over interstate access services") (emphasis in original).

but is not a "conferral[] of authority."[9] Section 251(g) provides no independent basis for the Commission to exercise authority with respect to matters over which it had no jurisdiction prior to the 1996 Act.

As the tortured history of intercarrier compensation for the transport and termination of traffic destined for Internet Service Providers makes clear,[10] the Commission risks prolonged industry uncertainty if it attempts to achieve policy objectives at the expense of clear legal sustainability. It is imperative in this time of general economic turmoil that any Commission decision with respect to intercarrier compensation be based upon a well-grounded and unimpeachable legal analysis of the statutory framework.

Moreover, while the Proposals suggest that the Commission intends to accomplish reform "by electing to partner with the states,"[11] the Proposals take no account of the strict jurisdictional fence imposed by Section 2(b). Section 2(b) of the Act has been characterized as a "hog tight, horse high, and bull strong" jurisdictional fence,[12] preventing the Commission from preempting state law or engaging in the regulation of intrastate telecommunications matters except in very limited circumstances such as pursuant to a clear Congressional mandate or a finding that the interstate and intrastate components of regulation are inseparable.[13] No such explicit mandate or

[9] *AT&T Corp. v. Iowa Utils. Bd.*, 525 U.S. 366, 381 n.8 (1999).

[10] *See Implementation of the Local Competition Provisions in the Telecommunications Act of 1996; Intercarrier Compensation for ISP-Bound Traf*fic, Declaratory Ruling and Notice of Proposed Rulemaking, 14 FCC Rcd. 3689 (1999) ("ISP Declaratory Ruling"), *vacated and remanded, Bell Atlantic Tel. Cos. v. FCC*, 206 F.3d 1 (D.C. Cir. 2000); *ISP Remand Order*, 16 FCC Rcd 9151, *remanded, WorldCom v. FCC*, 288 F.3d 429 (D.C. Cir. 2002), *cert. den.*, 538 U.S. 1012 (2003).

[11] Proposal A, ¶ 207; Proposal C, ¶ 202.

[12] *Iowa Utils. Bd. v. FCC*, 120 F.3d 753, 800 (8th Cir. 1997).

[13] *Louisiana PSC*, 476 U.S. at 368-69, 374-76 and n.4.

finding is referenced in the Proposals as drafted.[14] In *Louisiana v. PSC*, the Supreme Court stated, "In our view, the jurisdictional limitations placed on the [Commission] by § 152(b), coupled with the fact that the Act provides for a 'separations' proceeding to determine the portions of a single asset that are used for interstate and intrastate service, 47 U.S.C. § 410(c)" defeated the theories that Congress had clearly expressed an intent to displace state law or that state regulation would frustrate federal policy.[15] The mere fact that state regulation *might* interfere with furtherance of an interstate goal provides insufficient cause to overcome the limitations of Section 2(b).

In light of the fence erected by Section 2(b) and the fact that Section 251(g) does *not* extend to intrastate matters, the Commission cannot rely upon Section 251(g) to bring intrastate access traffic within the scope of its unified intercarrier compensation framework.

2. <u>Sections 251 and 252 Do Not Provide the Commission with Authority to Mandate Intrastate Rate Reductions as Part of any Transition.</u>

Even if the Commission can articulate a statutory basis for overcoming the Section 2(b) hurdle and unifying all rates pursuant to Sections 251 and 252, it does not have authority to mandate reductions in intrastate access charges or any other intrastate rates in advance of Section

[14] Although Proposals A and C address Verizon's arguments that Section 251(b)(5) is not limited to traffic exchanged between two LECs in a local calling area, they do not mention, let alone analyze or rebut, the state commissions' and other parties' Section 2(b) arguments. *See Ex Parte* Letter from James Bradford Ramsey, General Counsel, NARUC, to Marlene H. Dortch, Secretary, FCC, Docket Nos. 01-92, 08-152, 04-36, 06-122, 05-194 & 80-286, at 4-5 (filed Oct. 17, 2008); *Ex Parte Letter from* Daniel Mitchell, Vice President, Legal & Industry, National Telecommunications Cooperative Association, to Marlene H. Dortch, Secretary, FCC, Docket Nos. 01-92, 05-337, 96-45 & 04-36 (filed Oct. 17, 2008). *See also Developing a Unified Intercarrier Compensation Regime*, CC Docket No. 01-92 *et al.*, Comments of NTCA, at 2 (Sept. 18, 2008).

[15] *Louisiana PSC*, 476 U.S. at 369. In light of Section 410, it is unclear how the Commission could mandate revisions to intrastate access charges without referral first to the Federal-State Joint Board for consideration of allocation of costs and revenues between the interstate and intrastate jurisdictions. *See* 47 U.S.C. § 410(c) ("The Commission *shall* refer any proceeding regarding the jurisdictional separation of common carrier property and expenses between interstate and intrastate operations … to a Federal-State Joint Board ….") (emphasis added).

252(d)(2) pricing proceedings by the state commissions. The proposed transition plan, which would require near-term reductions in intrastate access charges before any pricing determinations are made by state commissions, is therefore unlawful. Indeed, the Commission has been down this path before with unfavorable results. In its 1996 *Local Competition Order*, the Commission adopted a cost methodology for state commissions to use in pricing transport and termination functions under Section 252(d)(2).[16] But it also prescribed "default proxies" for transport and termination rates because of the concern "that it may not be feasible for some state commissions conducting or reviewing economic studies to establish transport and termination rates" using the Commission's methodology in a timely manner.[17]

On appeal, the proxy prices were vacated because "[s]etting specific prices goes beyond the [Commission's] authority to design a pricing methodology," and such an approach was found to "intrude[] on the states' right to set the actual rates" under Section 252(d)(2).[18] Thus, it has been clear for over a decade that the Commission has no authority to prescribe specific transport and termination rates. The fact that such rates might be "proxy," "interim," or "transitional" in nature does not save them – the rate-setting limitations identified by the Supreme Court and the Eighth Circuit apply regardless. In fact, when the Commission adopted its proxy prices in 1996, it did so precisely because it believed an "interim" solution was necessary and appropriate pending the completion of TELRIC rate cases by the state commissions.[19] The mere fact that the

[16] *Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, First Report and Order, 11 FCC Rcd 15499, 16024, ¶ 1056 (1996) ("Local Competition Order").

[17] *Id*. at 16026-16028, ¶¶ 1060-1062.

[18] *Iowa Utils. Bd. v. FCC*, 219 F.3d 744, 757 (8th Cir. 2000), *aff'd in part and rev'd in part*, *Verizon Comm's, Inc. v. FCC*, 535 U.S. 467 (2002), and *vacated in part*, *Iowa Utils. Bd. v. FCC*, 301 F.3d 957 (8th Cir. 2002).

[19] *Local Competition Order*, 11 FCC Rcd at 15883, ¶ 767. ("A proxy approach might provide a faster, administratively simpler, and less costly approach to establishing prices *on an interim basis* than a detailed forward-looking cost study.") (emphasis added).

prices were interim did not sway the Eighth Circuit from its decision to vacate: "It is clear from the language of the [*Local Competition Order*], as well as the rules, that the state commissions are to use the proxy prices until the state commissions have established their own rates using the TELRIC method. The use of the proxy prices until such time is not optional."[20] The very same is true of the transitional rates proposed by the Commission here – the proposals would impermissibly prescribe rate reductions before completion of the state commission rate-setting proceedings contemplated by Section 252. It would also be legally unsustainable for the FCC to direct state commissions to conduct abbreviated proceedings to establish interim rates for CLECs without providing them due process to justify their rates under the 252(d)(2) standards.

In sum, any transition plan that includes mandatory reductions in intrastate rates is doomed to fail for the same reason that the proxy prices were rejected a decade ago.[21] Rather than tread back down this path, if the Commission is concerned (as it should be) about the impact on the industry of a transition from current intrastate access and reciprocal compensation rates to a new (presumably lower) unified rate, a better course is to delay the implementation of new rates altogether for at least two years, giving affected carriers the opportunity to build into their business plans the anticipated impact of the new system and provide the states time to begin conducting the required proceedings.[22] In order to be legally sustainable, states must determine the step-down in rates in the transition period that begins two years after the effective date of the Commission's order.

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[20] *Iowa Utils. Bd. v. FCC*, 219 F.3d at 757.

[21] Because Section 251(g) is not a substantive grant of authority and does not encompass intrastate access charges, the Commission may not rely on that section as authority for establishing transition rates either.

[22] In the event that the Commission may conclude that it has authority to adopt a transition and proceed to do so, the Joint Commenters also provide recommendations with respect to a proper transition in section II.B.1 below.

3. The Commission's Proposed Transitional Intrastate Rate Reductions Are Arbitrary and Capricious.

Even if the Commission had authority to sweep intrastate access charges within its reform proposals and to mandate rate reductions as part of a transition pursuant to Sections 251 and 252, the proposed rate reductions are arbitrary, capricious, and likely to fail upon appeal. For example, the Proposals provide no basis or context for the "50 percent reduction" in the difference between intrastate and interstate access charges in each of the first two years after the order becomes effective.[23] The same is true of the separate "50 percent reductions" that would apply to terminating rates in the third and fourth years after the order becomes effective.[24] In both cases, the "50 percent" figure appears to have been plucked from thin air without explanation or context in the interest of achieving rate reduction milestones by dates certain.

Although the Commission's interpretation of the Act is entitled to some deference when filling "gaps" in ambiguous statutes,[25] the Commission has provided no statutory tether whatsoever for the proposed reductions. Even if the Commission had authority to go beyond establishment of a methodology and to set rates – which it does not, as discussed above – it must have some reasonable basis for the rates that it sets[26] and must follow proper processes to establish lawful rates.[27] In the present case, however, the Proposals would prescribe transitional rates

[23] Proposal A, ¶ 193; Proposal C, ¶ 188.

[24] Proposal A, ¶ 194; Proposal C, ¶ 189.

[25] *See, e.g., National Cable Telecomms. Ass'n. v. Brand X Internet Services*, 545 U.S. 967, 981 (2005).

[26] *See, e.g., Alltel Corp. v. FCC*, 838 F.2d 551, 556-57 (D.C. Cir. 1988) (citations omitted) (finding that while the Commission has "broad discretion in its choice of methods for the determination of rates," it must provide a "reasoned explanation" for such determinations); *Nader v. FCC*, 520 F.2d 182, 192 (D.C. Cir. 1975) (citations omitted) (stating that the Commission's responsibility in rate investigations is to determine what is "just and reasonable," and that in reviewing such decisions, "there is a 'zone of reasonableness' within which the Commission's determination must be upheld").

[27] *See, e.g., Virgin Islands Tel. Co. v. FCC*, 444 F.3d 666, 669-70 (D.C. Cir. 2006) (discussing the statutory and regulatory processes by which tariffed rates may be found "just and reasonable" within the

without any statutory authority or any explanation of why or how the specific rates were chosen. Such arbitrary rate-setting is unlikely to survive judicial scrutiny.[28]

B. A New Approach to Intercarrier Compensation (V.B.2.)

1. Transition Period Should Be Modified to Account for Market Realities; States Should Reduce Intrastate Access Rates to Interstate Levels, If Appropriate, Over a Five-year Period

Even apart from the legal issues discussed above, the two-year transition period for moving intrastate access rates to interstate levels is too short for most states. It ignores and/or misstates important facts about CLECs' access rates and their ability to revise retail rates. The Commission should adopt a standstill period of at least two years from the effective date to allow the industry sufficient time to modify business plans. This is especially critical in light of the current economic downturn, which some have said may be a once in a lifetime period of economic turmoil. The Commission should adopt a five-year transition period, which begins at the end of the standstill period, to move intrastate access rates to interstate levels. The reality of the competitive telecommunications market prohibits any shorter transition periods.

Rather than arbitrarily pick steps for each phase of the transition, the Commission should direct states to determine the step-down in rates. The states are best situated to evaluate the difference between intrastate and interstate rates and the impact of reductions on carriers operating within each state. PAETEC, for example, would experience significant access revenue reductions at the end of the first two years of the Proposals (as currently drafted).[29] Telepacific,

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meaning of Section 201(b) and therefore "substantively lawful"); *Nader*, 520 F.2d at 205 (stating that the "essential elements" of a rate prescription order "are a full opportunity to be heard and a finding that the action taken is just and reasonable").

[28] The Commission's approach is especially infirm since interstate terminating rates may already be below the 252(d)(2) rates that a CLEC may be justified in charging.

[29] Declaration of William A. Haas, ¶ 7 (attached hereto as Attachment A; a non-redacted, confidential version is also being filed separately under seal). *See also* Declaration of Joseph O. Kahl, ¶ 6 (at-

which operates primarily in California, on the other hand, has intrastate rates that are much closer to interstate rates and therefore the California Commission may determine that the smaller delta enables a shorter transition after the two-year standstill period.

The two-year standstill and a reasoned glide path that takes into account rate differentials in each state are necessary in part because, contrary to the assumptions in the Proposals, CLECs cannot make up this lost revenue at the drop of a hat. First, most CLECs serving business customers have long-term customer contracts that preclude unilateral retail rate increases. For example, PAETEC's average customer contract length is approximately four years.[30] Second, some state commissions have prevented CLECs from including "change of law" provisions in their customer contracts.[31] Thus CLECs do not have the unfettered freedom suggested by Proposals A and C to increase retail rates to make up for lost intercarrier compensation revenue.[32] Third, some CLECs do not have the ability to offset access reductions with increases in SLCs.[33] Finally, most carriers have already finalized their budgets and business plans for 2009. As such, the Commission should not begin implementing any intercarrier compensation changes until the beginning of 2011 (or two years from the effective date) and it should direct the states to evaluate and determine how quickly intrastate rates should be reduced to interstate levels, or to some other appropriate interim level.

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tached hereto as Attachment B, a non-redacted, confidential version is also being filed separately under seal).

[30] Declaration of William A. Haas, ¶ 5. *See also* Declaration of Joseph O. Kahl, ¶ 5.

[31] Declaration of William A. Haas, ¶ 5.

[32] "As discussed above, competitive carrier end-user charges are not subject to rate regulation, and those carriers have the opportunity to recover lost access revenue through any legally permissible means." Proposal A, ¶ 319, Proposal C, ¶315. *See also* Proposal A, ¶ 318; Proposal C, ¶ 314 ("Unlike incumbent LECs, competitive carriers (e.g., such as competitive LECs, CMRS providers, and non-dominant IXCs) lack market power and are considered non-dominant. As a result, their end-user charges are not subject to comparable rate regulation by the Commission and the states.").

[33] Declaration of William A. Haas, ¶ 6.

2. Terminating Rates Should Vary by Company

The Commission should not mandate a uniform statewide rate. Under current law, most states have established terminating access and reciprocal compensation rates that vary based on the ILEC and/or CLEC providing service within the state. Enormous differences exist among service providers due to differing economies of scale, as well as the provision of different services, geography, and other operational characteristics. A uniform state-based rate would not reflect these legitimate cost and market distinctions.[34]

Although intercarrier compensation rates should be based on an individual carrier's forward looking costs, implementation of safe harbor benchmarks is an acceptable approach provided the benchmarks are reasonably reflective of a carrier's costs. As PAETEC has shown, neither AT&T nor Verizon provide a reasonable benchmark for any carrier, including PAETEC. Although $0.0007 may be an appropriate rate for large, integrated RBOCs, "a rate equal to $0.0007 would fall far short of properly compensating" a CLEC, such as PAETEC or RCN, "for the capital it has deployed and the legitimate expenses it incurs in transporting and switching voice-related services."[35] Any order that requires CLECs to provide below-cost termination services to IXCs and shift the un-recovered costs of IXC traffic termination to their local end user customers violates the Act.[36] Based on similarities in network and other cost related factors, CLECs should be benchmarked to mid-size ILECs.[37]

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[34] *See, e.g., Ex Parte* Letter from Tamar E. Finn, Counsel to PAETEC, to Marlene H. Dortch, Secretary, FCC, Docket No. 01-92 (filed Oct. 17, 2008) ("*PAETEC/QSI Analysis Letter*") (advocating that intercarrier compensation rates should be based on an *individual carrier's* forward looking costs).

[35] *See id*., Exhibit 1 (Declaration of Michael Starkey, QSI Consulting), at 7.

[36] *See id*., at 2.

[37] *See id.*, at 1.

Given the variables inherent in network design between CLECs, ILECs and other service providers, the Commission should require states to undertake a carrier-specific review for purposes of terminating rates, not a state-wide approach, which would have the result of ignoring CLEC network architecture and over-emphasize large RBOC economies of scale. Although the Commission could permit benchmarking CLEC rates to ILEC rates as is the current practice under Section 251(b)(5), CLECs should be benchmarked to mid-sized LECs.

3. The Commission Should Not Abrogate the Single POI per LATA Rule by Adopting New Edge Rules

The Commission should not adopt the "edge rules" because they would undercut current interconnection rules without adequate or reasoned justification and place competitive carriers at a significant disadvantage.

As Proposals A and C recognize, "[t]he reciprocal compensation rules currently require the calling party's LEC to compensate the called party's LEC for the additional costs associated with transporting a call subject to section 251(b)(5) *from the carriers' interconnection point to the called party's end office*, and for the additional costs of terminating the call to the called party."[38] Although these Proposals purport not to change current interconnection rules, the network "edge" concept would in fact upset existing arrangements. At the end of the transition period, CLECs could see their interconnection costs increase substantially while RBOCs would experience no increase.

A simple example illustrates the effects of the "edge" proposal. Assume that the RBOC has three tandems in LATA XYZ while the CLEC has a single switch serving that LATA. The

[38] Proposal A, n.444; Proposal C, n.435 (emphasis added). *See also* 47 C.F.R. § 51.701(c) ("transport is the transmission and any necessary tandem switching of telecommunications traffic subject to section 251(b)(5) of the Act from the interconnection point between the two carriers to the terminating carrier's end office switch…").

CLEC has established a single point of interconnection ("POI") at one of those three RBOC tandems and pays reciprocal compensation to the RBOC for each minute of use ("MOU") it hands to the RBOC at the POI. Under the Proposals, that compensation rate would step down over a period of ten years. But, in year eleven, the RBOC can designate each of its tandems as an "edge" and *require the CLEC to pay dedicated transport from the POI to each of the other two tandems, in addition to the new terminating rate*. Moreover, unless the Commission clarifies its rules, RBOCs will continue to fight the obligation to provide dedicated transport on a single trunk group at TELRIC rates for all traffic,[39] further increasing the CLEC's costs. On the other hand, the CLEC has only one switch in LATA XYZ and therefore cannot designate additional edges or require the RBOC to pay additional transport. Based on these differences in network architecture, the CLEC's costs increase markedly when the edge rule is implemented, but the RBOC's costs do not.

The network edge rule is inconsistent with the plain text of the Act. Section 251(c)(2) requires ILECs to provide interconnection at any technically feasible point requested by CLECs. Proposals A and C[40] ignore Congress' choice. Instead, as initially described by Verizon, they grant any terminating carrier the right to demand "at least one [point of interconnection ("POI")] per LATA" and up to as many POIs as the terminating carrier may desire, so long as it does not

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[39] *See Petition of Worldcom, Inc. Pursuant to Section 252(e)(5) of the Communications Act for Pre-emption of the Jurisdiction of the Virginia State Corporation Commission Regarding Interconnection Disputes with Verizon Virginia, Inc. and for Expedited Arbitration*, Memorandum Opinion and Order, 17 FCC Rcd 27039, ¶¶ 172-77, 215-217 (Wireline Comp. Bureau 2002) ("*Virginia Arbitration Order*"). *See also* Petition of AT&T, Inc. for Interim Declaratory Ruling and Limited Waivers, WC Docket No. 08-152, n.79 (filed July 17, 2008) (expressing AT&T willingness to *negotiate* arrangements under which CLECs can use single interconnection facility to terminate local and interexchange traffic).

[40] *See* Proposal A, ¶ 275; Proposal C, ¶ 270.

exceed the number of ILEC tandems in that LATA.[41] The Proposals argue that they are not inconsistent with the Act and attempt to distinguish a single physical POI from multiple financial POIs.[42] To the contrary, as the Chief of the Wireline Competition Bureau has summarized, a proposal to establish a single POI in each LATA "more closely conforms to the Commission's current rules" than a proposal to transfer financial responsibility through multiple virtual POIs throughout a LATA.[43] The current rules recognize and account for differences in RBOC and CLEC network technologies to prevent conferring a competitive advantage on RBOC networks.[44] The edge proposal does just the opposite; it confers a regulatory advantage on RBOCs. The Proposals give no principled reason why the Section 251(b)(5) rate should apply at the point of interconnection and cover all transport and termination functions from the POI to the end user for the ten year transition period but then be abandoned when all traffic is unified at a single 251(b)(5) rate. Adopting the edge proposal would reverse policy, without the adequate justification required by law.[45]

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[41] *Ex Parte* Letter from Susanne A. Guyer, Verizon, to Chairman Martin, *et al.*, CC Dockets Nos. 01-92 and 96-45, at 1-2 (filed Sept. 12, 2008).

[42] *See* Proposal A, n.726; Proposal C, n.717.

[43] *Virginia Arbitration Order*, 17 FCC Rcd 27039, 27063-65, ¶¶ 51-53. The Commission declined to address in at least one other proceeding the question of whether so-called financial interconnection points could satisfy the requirements of the Act. *See Application by Verizon Virginia, Inc., Verizon Long Distance Virginia, Inc., Verizon Enterprise Solutions Virginia, Inc., Verizon Global Networks, Inc., and Verizon Select Services of Virginia, Inc. for Authorization to Provide In-Region, InterLATA Services in Virginia*, Memorandum Opinion and Order, 17 FCC Rcd 21880, 21977, ¶ 173 (2002) (finding that Verizon had satisfied its interconnection obligations by entering into at least one interconnection agreement that did not mandate multiple points of interconnection for financial responsibility purposes).

[44] *See e.g., Local Competition Order* at ¶ 202.

[45] "[A]n agency choosing to alter its regulatory course 'must supply a reasoned analysis indicating that its prior policies and standards are being deliberately changed, not casually ignored.'" *Action for Children's Television v. FCC*, 821 F.2d 741, 745 (D.C. Cir. 1987) (quoting *Greater Boston Television Corp. v. FCC*, 444 F.2d 841, 852 (D.C. Cir.1970)).

4. The Commission Should Clarify that Classification of IP-PSTN Services As Information Services Does Not Affect LEC Section 251 and 252 Rights and Duties

If the FCC classifies interconnected VoIP services, computer-to-phone services,[46] or any other *services* that touch the PSTN as an information service, it must affirm explicitly that LECs' Section 251 and 252 obligations continue to apply.[47] The technology used by a LEC's customer (or the LEC) to provide an information service should be of no consequence to the fundamental interconnection rights and duties associated with the telecommunications input used by the information service to exchange calls with the public network. As the Commission recognizes, in order to exchange traffic on the public network, some telecommunications must underlie the information service. For example, AT&T and Verizon cannot escape their obligation to exchange traffic with other carriers because they move their customers to fixed VoIP services. Congress passed landmark legislation in 1996 opening local markets to competition; it surely did not intend for this achievement to be nullified by ILECs migrating their end user customers to what would now be classified information services. The reality is that telecommunications traffic was carried in IP format since well before the 1996 Act was adopted. The only change is that more traffic is now being carried exclusively in that format. Congress was certainly aware of this format when the Act was adopted.

[46] *See generally Federal-State Joint Board on Universal Service*, Report to Congress, 13 FCC Rcd 11501 (1998) ("*Stevens Report*").

[47] *See Ex Parte* Letter from Russell M. Blau, Counsel to Covad and PAETEC, to Marlene H. Dortch, Secretary, FCC, Docket No. 01-92, Covad Communications Ex Parte Presentation, at Attachment 2 (PAETEC Attachment) (filed Oct. 28, 2008); *Ex Parte* Letter from 360networks(USA), Inc., *et al.* to Kevin Martin, Chairman, FCC, Docket Nos. 01-92 & 04-36 (filed Sept. 29, 2008); *Ex Parte* Letter from Thomas Jones, Counsel for tw telecom, *et al.*, to Marlene H. Dortch, Secretary, FCC, Docket Nos. 05-337, 99-68, 04-36, 01-92 & 96-45 (filed Oct. 24, 2008).

The Commission therefore should re-affirm the *Time Warner Order*[48]and make clear that it applies to all LECs. VTel has shown the need for reaffirmation of CLEC's 251 and 252 rights when they provide telecommunications service to VoIP and other information service providers.[49] The *Time Warner Order* emphasized that "the statutory classification of a third-party provider's VoIP service as an information service is irrelevant to the issue of whether a wholesale provider of telecommunications may seek interconnection under Section 251(a) and (b)."[50] The *Time Warner Order* reiterated a long line of cases holding that Section 251 does not differentiate between the provision of retail or wholesale service.[51] The principles of *Time Warner Order* apply with equal if not greater force if the Commission classifies VoIP services as information. Information service providers are permitted to purchase local business services to connect to the PSTN.[52] In short, they are end-user customers of a LEC's retail telecommunications services.

But the Commission must go further than it did in *Time Warner* if it classifies fixed VoIP services as information services. Absent further clarification, ILECs will argue that CLECs are

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48 *Time Warner Cable Request for Declaratory Ruling*, Memorandum Opinion and Order, 22 FCC Rcd 3513 (2007) ("*Time Warner Order*").

49 *See, e.g., Petition for Declaratory Ruling Whether Voice over Internet Protocol Services Are Entitled to the Interconnection Rights of Telecommunications Carriers*, Petition for Declaratory Ruling (filed April 11, 2008) ("VTel Petition").

50 *Time Warner Order*, ¶ 15.

51 *Id.* ¶ 9.

52 *See Amendments of Part 69 of the Commission's Rules Relating to Enhanced Service Providers*, Order, 3 FCC Rcd. 2631, 2633, ¶ 20 & n.53 (1988) ("At present, enhanced service providers are treated as end users and thus may use local business lines for access for which they pay local business rates and subscriber line charges."). *See also Amendments of Part 69 of the Commission's Rules Relating to the Creation of Sub-elements for Open Network Architecture*, Notice of Proposed Rulemaking, 4 FCC Rcd. 3983, 3987-89 & n.71 (1989) (noting that "[t]he access charge exemption for enhanced services is implemented by treating ESPs as end users for the purposes of Part 69."); *Access Charge Reform; Price Cap Performance Review for Local Exchange Carriers; Transport Rate Structure and Pricing End User Common Line Charges*, First Report and Order, 12 FCC Rcd. 15982, ¶ 348 (1997) ("We therefore conclude that ISPs should remain classified as end users for purposes of the access charge system.").

not entitled to 251(a) and (b) rights *to reach the ILEC's VoIP customers* in their effort to force CLECs to sign significantly more costly commercial agreements, just as they do now with respect to IP interconnection and commercial UNE-P replacement services. The basis for keeping interconnection with ILEC VoIP customers subject to Sections 251(a) & (b) is clear. Even where the LEC is the provider of the information service, some telecommunications must underlie that service if it is going to interconnect with the public network and it is that "telecommunications" that enables the Commission "to bring IP/PSTN traffic within the section 251(b)(5) framework."[53] Under Commission precedent, a provider is classified based on each service it offers.[54] In the case of a LEC offering an information service with PSTN connectivity, the LEC is providing both an information service and the "telecommunications" that permits the information service to connect to the PSTN. In short, the LEC is providing wholesale telecommunications to itself in order to provide its end user an information service with PSTN connectivity. It is this "telecommunications" offering that obligates the LEC to comply with Sections 251(a) & (b).

The Commission must also go beyond *Time Warner* to affirm that LECs retain rights and obligations under Section 251(c) and 252, including but not limited to 251(c)(2) & (3), when providing telecommunications to their information service provider customers. Although Section 252(c)(2) uses the narrower terms telephone exchange service and exchange access, information service providers use these services just as any other business customer to connect to the PSTN. When LECs exchange telecommunications traffic—regardless of whether either LEC's customer

[53] Proposal A, ¶ 218 & n.564; Proposal C, ¶ 213 & n. 555.

[54] "[A] single entity can be both a telecommunications provider and an information services provider," with the classification depending on the service offered. *See Third Computer Inquiry, Phase II*, Memorandum Opinion and Order on Reconsideration, 3 FCC Rcd 1150, n.77 (1988) ("*Computer III*").

is an information service provider—it is exchanging telephone exchange service or exchange access traffic and is entitled to interconnection under Section 251(c)(2).

Remaining silent on these issues, as Proposals A and C do, will result in endless litigation and disputes that would undermine the market opening provisions of the 1996 Act. The 1996 Act was designed not only to open local markets to competition, but also to spur advances in network technologies. As the PSTN moves from circuit-switched to managed packet networks, AT&T and Verizon cannot rely on this transition to escape the market opening obligations of Sections 251 and 252. The Commission must make clear that these 251 and 252 rights and obligations apply in both directions—the exchange of traffic between an RBOC VoIP or information service provider customer and a CLEC's VoIP or information service provider customer.

Finally, the Commission must fix the classification language in Proposal A paragraph 209,[55] which arguably contains a loophole big enough to drive the entire PSTN through. That paragraph provides that the FCC intends to "classify as 'information services' those services that originate calls on IP networks and terminate them on circuit-switched networks, or conversely that originate calls on circuit-switched networks and terminate them on IP networks (collectively 'IP/PSTN' services)."[56] The fact that a circuit-switched customer may complete some calls to an IP-based customer should not result in that entire circuit-switched service being classified as an information service. Presumably the Commission intended to address AT&T's argument that it is inconsistent *for intercarrier compensation purposes* to subject IP-PSTN calls to reciprocal

[55] *See also* Proposal C, ¶ 204 ("We now classify as 'information services' those services that originate calls on IP networks and terminate them on circuit-switched networks, or conversely that receive calls from circuit-switched networks and terminate them on IP networks (collectively 'IP/PSTN' services). Such traffic today involves a net protocol conversion between end-users, and thus constitutes an 'enhanced' or 'information service.'").

[56] Proposal A, ¶ 209; Proposal C, ¶ 204.

compensation and PSTN-IP calls to access charges.[57] Without conceding this point, it is clear that a PSTN service should not be classified as an information service just because the end user occasionally calls an IP-based customer. If adopted, the following clarification should be added to paragraph 209:

> <u>We clarify, however, that a circuit-switched telecommunications service does not become "information" merely because some portion of the calls originated by that service may be destined to terminate on IP networks, or vice versa; only those calls that actually originate or terminate on IP networks constitute information services.</u>

C. Additional Costs Standard (V.B.4.)

1. <u>The Commission Should Not Replace TELRIC With an Incremental Cost Standard</u>

As explained in the Declaration of August H. Ankum, Ph.D. and Olesya Denney, Ph.D. on Behalf of PAETEC,[58] the proposal to revise the cost methodology for terminating intercarrier compensation rates is results-oriented, incomplete, internally inconsistent, and riddled with inaccuracies. For example, while the Commission's preferred outcome (a rate "extremely close to zero") might be expected under a *short-run* marginal cost standard, it is inconsistent with the Commission's decision to rely on *long-run* incremental costs. The desire to drive intercarrier compensation rates toward zero cannot outweigh sound economic analysis. Yet in order to reach the desired result, the Proposals ignore or minimize the substantial incremental costs of installing and operating softswitch-based networks. The proposed methodology also is based on the costs of terminating *all* traffic in a state. But in the real world, there is no network that enjoys the benefits of scale and capacity to support a conclusion that such a massive amount of traffic could

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[57] *See generally* Petition of AT&T for Declaratory Ruling and Limited Waivers, WC Docket No. 08-152 (filed July 23, 2008).

[58] Declaration of August H. Ankum, Ph.D. and Olesya Denney, Ph.D., QSI Consulting, Inc., on Behalf of PAETEC, CC Dockets 01-92 et al. (filed Nov. 26, 2008) ("Ankum/Denney Declaration").

possibly be terminated at the near zero costs that the Commission envisions. Furthermore, certain assumptions regarding traffic-sensitivity and interconnection costs are simply incorrect. Finally, the "available evidence" that ostensibly supports the low-cost (or no-cost) result is limited to AT&T's in-house economist's analysis of rural carrier network costs in a single state under very different cost assumptions than proposed by the Commission in the current proceeding.

By contrast, the TELRIC standard is time-tested, theoretically sound, and the pricing model used for the inputs that LECs use to perform terminating functions. As the Commission considers substantial reforms to the structure of intercarrier compensation, it should not experiment with a new cost standard that will determine the rate for one of the most significant economic issues affecting the telecommunications industry. There are far too many questions with respect to developing and implementing the proposed new standard -- questions that (unlike the 1996 order and subsequent clarifications) the current proposal leaves unasked and/or unanswered. The Commission should therefore reject its extreme version of the Faulhaber approach and affirm that states should continue using TELRIC to set Section 251(b)(5) compensation rates.

2. If the Commission Nevertheless Adopts the New Standard, the Rate Should Only Apply to IP-IP Interconnection

To the extent that the Commission replaces TELRIC with an incremental cost standard that is based on a network that deploys only softswitches and fiber transport, it must condition that rate on the originating LEC agreeing to IP-IP interconnection handoffs. Applying the rate when traffic is handed off to the terminating carrier in TDM format ignores the costs the terminating carrier incurs to convert the traffic to IP.[59] If a LEC refuses to hand off traffic to the terminating carrier via a direct IP-IP interconnection, it should be subject to a higher terminating

[59] Ankum/Denney Declaration, ¶ 48.

rate. The Commission must also declare that IP-IP interconnection is a technically feasible method of interconnection under Section 251(c)(2) and is subject to 252.

3. The Commission Lacks Statutory Authority to Dictate the Results of a State Commission 252(d)(2) Cost Proceeding

Proposals A and C go well beyond the boundaries of adopting a cost methodology and are unlikely to survive judicial review. Because the Proposals specify the inputs state commissions must use and dictate the resulting rate, they run afoul of the same statutory limitations that doomed the proxy prices established in the *Local Competition Order*.[60]

The Supreme Court's *Iowa Utilities Board* decision restricts how far the Commission can go in establishing a pricing methodology, and the Proposals clearly cross that line.[61] By requiring state commissions to use the forward-looking network design of softswitches and fiber transport,[62] and threatening to set the rate if the state commission proceeding does not result in a rate close to zero,[63] the Proposals do not allow the state commissions to "determin[e] the concrete result." As drafted, the Proposals put the states in the position of doing little more than ratifying the Commission's rate-setting mandate.

Several Justices believed the Commission exceeded its authority by requiring state commissions to employ a TELRIC methodology. For example, Justice Breyer disputed the

[60] Following remand from the Supreme Court, the United States Court of Appeals for the Eighth Circuit vacated the Commission's default proxy prices, relying upon the higher court's determination that the Commission's role was limited to resolving "general methodological issues," finding that "[s]etting specific prices goes beyond the [Commission's] authority to design a pricing methodology," and concluding that such an approach would "intrude[] on the states' right to set the actual rates." *Iowa Utils. Bd. v. FCC*, 219 F.3d at 757.

[61] *AT&T v. Iowa Utils. Bd.*, 525 U.S. 366, 384 (1999) (emphasis added).

[62] *See* Proposal A, ¶ 272; Proposal C, ¶ 267 ("We offer further guidance regarding specific aspects of these cost studies. First, these cost studies must use the least cost, most efficient network technology. We find that the least cost, most efficient switch today is a softswitch. We further find that the least cost, most efficient technology for transport is fiber optic cable. We observe that, when carriers deploy fiber, they typically deploy capacity significantly in excess of current needs.").

[63] Proposal A, ¶ 215; Proposal C, ¶ 215.

Commission's argument that TELRIC was merely a "pricing standard": "Most importantly, the FCC's rules embody not an effort to circumscribe the realm of reasonable, but rather a policy-oriented effort to choose among several different systems, including systems based upon actual costs or price caps. … [T]hey constitute the kind of detailed policy-related ratesetting that the statute in respect to local matters leaves to the States."[64] Moreover, the Eighth Circuit, in confirming the Commission's authority to resolve "general methodological issues,"[65] cited the Commission's explanation of its TELRIC pricing standard as "a methodology for state commissions to use in completing the 'critical and complex task of determining the economic costs of an efficient telephone network.'"[66] Thus, as the Eighth Circuit ultimately determined, "it is the state commission's role to exercise its discretion in establishing rates."[67] Because the Proposals limit state commission discretion to choose inputs and are contrary to the principles by which this Commission defended TELRIC nearly a decade ago, they run significant risk of failure on appeal.[68]

D. Implementation (Direction to the States) (V.C.1.)

1. <u>LECs Must Be Permitted to Invoke a Change in Law to Revise Both Commercial Contracts and Interconnection Agreements</u>

The Commission should make clear that any adopted reforms constitute a change of law for both interconnection and traffic exchange agreements *and* commercial (retail and wholesale) contracts. As drafted, Proposals A and C state that the Commission's intercarrier compensation

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[64] *AT&T v. Iowa Utils. Bd.*, 525 U.S. at 424-427 (Breyer, J., dissenting) (citations omitted); *see also id*. at 407-411 (Thomas, J., dissenting).

[65] *Iowa Utils. Bd. v. FCC*, 219 F.3d at 757.

[66] *Id*. at 756 (quoting Reply Brief of the Federal Petitioners, Cases Nos. 97-826, *et al*. United States Supreme Court, at 7).

[67] *Id*. at 757 (citation omitted).

[68] *See also Federal Power Comm'n v. Hope Natural Gas Co.*, 302 U.S. 591, 602 (1944) (contrasting the "method employed" with the "result reached" in setting "just and reasonable" rates).

reforms constitute a "change in law" for purposes of interconnection agreements that "may contain change of law provisions that allow for renegotiation and/or may contain some mechanism to resolve disputes about new agreement language implementing new rules."[69] However, the Commission does not "abrogate existing contracts or otherwise allow for a 'fresh look' in light of our reforms;" and further states that it will leave this matter open to any change-of-law provisions that may be contained in these contracts, rather than requiring that they be reopened.[70] In many cases, states have prevented carriers from including change of law provisions in their commercial contracts.[71] As such, carriers with long-term contracts may have no ability to revisit and revise those contracts to take the Commission's reforms into account. The Commission should make clear that any adopted reforms constitute a change of law for both interconnection agreements and commercial (retail and wholesale) contracts, and that it preempts state authority to the extent the states prohibit carriers from making such modifications.

III. REFORM OF UNIVERSAL SERVICE CONTRIBUTIONS (IV.)

A. Contribution Assessment Methodology for Business Services (IV.B.3.)

1. Applying Three Different Reporting Methodologies Would Be Much Worse Than the Current System

The Commission's proposals to impose three separate reporting methodologies on service providers, based on numbers,[72] connections,[73] and revenues,[74] would be burdensome and would require substantial updates to accounting, billing, and collection systems.

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69 Proposal A, ¶ 292; Proposal C, ¶ 287.

70 Proposal A, ¶ 293; Proposal C, ¶ 288.

71 Declaration of William A. Haas, ¶ 5.

72 *See* Proposal A, ¶¶ 105-129; Proposal C ¶¶ 101-125.

73 *See* Proposal B, ¶¶ 78-82.

74 *See* Proposal A, n.373; Proposal B, n.239; Proposal C, n.364 (noting that TRS, LNP, and NANPA support will continue to be assessed through carrier revenue reporting).

Although the 499-A estimates that it takes on average 13.5 hours to complete, in Joint Commenters' experience it takes many more hours to compile the necessary information and complete the form. For example, it takes PAETEC approximately 20 hours to complete each of its Forms 499-A, and PAETEC has to complete a Form 499A for each of its three operating entities.[75] Adding two new reporting methodologies to this significant burden could exponentially increase the compliance cost for service providers making contributions to federal funding mechanisms. Even if the Form 499-A were "streamlined" to ask for total revenue (rather than intrastate, interstate, and international breakdowns), dividing revenue into the numerous line items on the Form is at least as onerous as the jurisdictional breakdowns. Most important, service providers would have to continue parsing revenue from bundled services into telecommunications and information categories, and would also have to break down each category of revenue into residential and business subtotals. This telecom/information distinction is one of the primary drivers behind adopting a numbers and/or connections basis for USF contributions and should be the basis for transitioning the other funds to a new contribution mechanism as well.

2. Hybrid Numbers and Connection Fees in Proposal B Would be Discriminatory and Inequitable to Small Businesses

The Joint Commenters oppose a hybrid numbers/connection system with high connection fees for small business services. Under the USF methodology included in Proposal B, carriers would be required to contribute:

- $0.85/month per number (residential & business, including wireless)
- $5.00/month per Business Connection, up to 64 kbps
- $35.00/month per Business Connection, above 64 kbps
- Mobile services are not "Assessable Connections"[76]

[75] Declaration of William A. Haas, ¶ 4.

[76] *See* Proposal B, ¶¶ 81-82.

This would be catastrophic for small businesses. For example, assume a small business uses one DSL line at $70.00 per month. Today, the USF contribution for that line would be approximately $8.05 (11.5% of the $70 monthly service charge). Under Proposal B, however, the USF contribution for that line would be $35 (and a total charge of $105 per month), resulting in a USF contribution increase of approximately 335%, and a total cost increase of 34.5% (from $78.05 to$105). The effective universal service contribution rate for that DSL line under Proposal B would be 50%.[77] Whether a small business uses a DSL service, or an integrated T-1 service that delivers voice, data, and Internet access services, the results are the same.[78] Small business bear the brunt of USF funding under Proposal B.[79]

Such a drastic rate increase, and resulting effective contribution rate, would be unlawful under the Act. Section 254(d) of the Act requires that the Commission establish universal service contributions on an "equitable and nondiscriminatory basis." Proposal B is inequitable to the extent that the contribution varies based on capacity, but small businesses purchasing a DSL connection would pay the same as an enterprise customer that utilizes a DS3 Internet connection.[80] Further, it is discriminatory, as it would require wireline and fixed wireless connections to pay contributions, but would not require contributions from mobile wireless connections, includ-

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[77] *See, e.g.*, *Ex Parte* Letter from Russell M. Blau, Counsel to Covad and PAETEC, to Marlene H. Dortch, Secretary, FCC, Docket No. 01-92, at Covad Communications Ex Parte Presentation (filed Oct. 28, 2008).

[78] *See generally Ex Parte* Letter from Stephen W. Crawford, General Counsel and Senior Vice President, Alpheus Communications, L.P., to Marlene H. Dortch, Secretary, FCC, Docket Nos. 06-122 & 96-45 (filed Oct. 228, 2008); *Ex Parte* Letter from Mary C. Albert, COMPTEL, to Marlene H. Dortch, Secretary, FCC, Docket No. 06-122 & 96-45 (filed Oct. 22, 2008).

[79] These added USF costs on small businesses would be in addition to the significant increase in retail rates that the FCC expects the LEC to be able to thrust onto the very same small business customer elsewhere in the proposals.

[80] *See id.*

ing broadband.[81] Finally, massive (50%) rate increases for small businesses are poor public policy generally, but especially so in these economic times. A 35% cost increase for DSL would force many businesses off the Internet. Proposal B would impact approximately 4.8 million business broadband users[82] to the tune of a $1 to 1.5 billion per year cost increase. Such a dramatic increase for small businesses would be unfair and contrary to the Act. Simply put, a $1 to $1.5 billion increase on small businesses would be both discriminatory and inequitable.

The Joint Commenters urge the Commission to simplify, rather than further complicate, the current assessment methodology.

3. The "No Assessable Numbers" Exception Swallows the Rule

The Commission should reject any broad exceptions to contributions based on numbers. The "no assessable numbers" exception included in Proposals A and C[83] is unfair, anti-competitive, and discriminatory to those service providers and customers that do not bundle voice and data services, or local and long distance services. Such a result violates the anti-discrimination provisions of the Act[84] as it would treat like services differently for purposes of USF and other regulatory fee assessments. It would also provide bundled service providers an artificial competitive advantage in the market.

The exception states, in part: "Prepaid calling card providers, *as well as any other current contributors who provide services to residential consumers but do not assign Assessable Numbers*, shall continue to contribute based on their revenues during the interim period until these

[81] *See id.*

[82] *See FCC, Trends in Telephone Service*, Table 2.2 (Total Advanced Service Lines) and Table 2.4 (Residential Advanced Service Lines), August 2008 (data as of June, 2007), *available at*: http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-284932A1.pdf.

[83] *See* Proposal A, n.329, Proposal C, n.321.

[84] *See* 47 U.S.C. § 254(d).

business services are assessed on the basis of connections and/or numbers." [Emphasis added.] One could read this confusing footnote to require every current USF contributor to treat as a business service any service it provides to a residential consumer that does not include an assigned number. This would wreak havoc on the numbers-based system and create severe competitive disadvantages for those providers that offer stand-alone services.

For example, if a residential customer purchases stand-alone DSL and "over-the-top" VoIP service from two different providers, that customer would pay a business rate contribution on the DSL service ($3.45 for a $30 DSL service with a contribution rate at 11.5%) in addition to a numbers-based contribution on the VoIP service ($1.00 for the VoIP phone number). But if another carrier bundled a telephone service with DSL, the customer would contribute only $1.00 for the assigned telephone number.

The same would apply to long-distance services offered to presubscribed residential users. If one carrier offered a bundled local and long distance service that included a number, the customer would pay only $1.00. But if the same customer purchased local service from one carrier and long distance service from another carrier, the customer would pay the local carrier $1.00 and the long distance carrier a revenue-based USF fee (11.5% of the interstate and international revenue).

The Commission should protect residential customers from being double-assessed USF fees when they obtain data and voice, or local and long distance, services from separate providers. The "no assessable numbers" exception to contributions based on numbers should be rejected.

B. Transition to New Methodology (IV.B.7.)

1. The Transition to a New Methodology Must Be at Least One Year

The Joint Commenters support a one-year transition to adjust reporting and billing systems to conform to any new universal service contribution requirements. The Commission's proposed six-month to one-year transition is a good start, given the complexity and cost to revise back office billing, collection, and accounting systems. This complexity will be exacerbated to the extent that the Commission imposes three separate contribution mechanisms on certain providers. The Joint Commenters, therefore, respectfully request that the Commission accompany any modification to the USF contribution and reporting requirements with a transition framework that allows a reasonable amount of time for carriers and other service providers to adjust their internal systems to comply with those new rules.

IV. FURTHER NOTICE OF PROPOSED RULEMAKING (VI.)

A. Intercarrier Compensation Further Notice (Originating Access) (VI.B.)

1. The FCC Does Not Have Legal Authority to End Intrastate Originating Access

Although the NPRM does not state clearly the statutory basis for ending intrastate access charges, it appears that the FCC may be relying on Section 251(g) as a substantive grant of authority to supersede intrastate access charges. As explained above, this is not a valid legal basis for usurping state commission jurisdiction over intrastate access charges.

2. The FCC Should Not End Originating Access Because It Would Be Inconsistent With The Calling Party Pays Regime That Governs Intercarrier Compensation

Sections 251/252 provide no basis or authority for regulation, reform, or elimination of *originating access charges*. Those sections permit the FCC to establish a methodology with respect to the "additional costs" of transporting and *terminating* telecommunications. The FCC interprets these sections as continuing the historical "Calling-Party-Network Pays" intercarrier compensation principle. While the FCC's proposed reforms aim to reduce the rates for such compensation, the underlying CPNP principle remains intact.

In the context of *a long-distance call*, CPNP requires that access charges be paid to the originating LEC for a long-distance call.[85] This is because the third party *IXC* (*not the originating LEC*) is the Calling Party Network. The IXC receives compensation from the caller for the carriage of the call. Thus, CPNP requires the IXC to pay both the terminating LEC *and the originating LEC* for the roles they play in helping to complete the call. It would be contrary to the CPNP framework underpinning 251/252 for the FCC to mandate elimination of originating access charges (whether interstate *or* intrastate) on interexchange traffic. If originating access charges were eliminated, the third party IXC would get a "free ride" on the originating end of every call, while properly paying compensation on the terminating side to the LEC for causing costs on the terminating LEC network. Thus, to avoid an arbitrary and capricious result and to apply the CPNP cost causation principles consistently *throughout* a more unified intercarrier compensation framework, the FCC cannot eliminate originating access charges.

3. If The FCC Nevertheless Reduces Originating Access, Any Phase Down Should Begin Only After Terminating Rates Are Reduced

The FCC should not reduce originating and terminating access rates at same time because of the substantial burden it will place on revenue recovery mechanisms (retail rates, SLCs, USF where available).

[85] Although Sections 251/252 bar originating charges on a local call, this is consistent with the Commission's CPNP principle -- the originating LEC, who receives compensation from its customer placing a call cannot recover originating charges from the terminating LEC for that call, and must instead *pay* the terminating LEC for the "additional costs" of terminating the call placed by the originating LEC's customer.

B. Other Issues (N/A)

1. Traffic Stimulation Rules Should Be Narrowly Tailored

If the goal is to thwart schemes that drastically increase *terminating* access traffic to take advantage of high access rates as suggested by the Commission in the intercarrier compensation proposals,[86] then the Commission should adopt rules, if any, that are narrowly tailored to address those wrongs, and those wrongs alone. The Commission's record contains no justification for modifying rules for CLECs that do not avail themselves of the rural LEC rate exemption.[87] Even Qwest and Sprint agree that any traffic stimulation rules should be limited to CLECs that elect the rural exemption or benchmark to rural rates.[88] Because of the numerous unintended consequences that could result from overbroad traffic stimulation rules,[89] if it takes action in this proceeding, the Commission should adopt narrow rules.

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[86] *See* Proposal A, ¶ 327; Proposal C, ¶ 323.

[87] *See Ex Parte* Letter from William A. Haas, Vice President Regulatory & Public Policy, PAETEC, Communications, Inc., to Marlene H. Dortch, Secretary, FCC, Docket No. 07-135, at 1 (filed June 12, 2008) ("PAETEC June 12, 2008 *Ex Parte*").

[88] *See Ex Parte* Letter from Melissa E. Newman, Vice President – Federal Regulatory, Qwest Communications International, Inc., to Marlene H. Dortch, Secretary, FCC, Docket No. 07-135, Attachment, at 1-2 (filed May 21, 2008) ("Qwest's most recent approach focuses on eliminating the impact of a proposed solution on innocent CLECs[]" by acknowledging that so-called traffic stimulators should be limited to charging the tariffed rate of the "nearest non-rural ILEC"); *Ex Parte* Letter from Norina Moy, Director, Government Affairs, Sprint Nextel, to Marlene H. Dortch, Secretary, FCC, Docket No. 07-135, at 1 (filed June 9, 2008) (The record also demonstrates that traffic pumping activity is now being perpetrated primarily by *certain* [CLECs] (emphasis supplied). *See also Ex Parte* Letter from Norina Moy, Director, Government Affairs, Sprint Nextel, to Marlene H. Dortch, Secretary, FCC, Docket No. 07-135, at 1 (filed July 30, 2008) ("[Sprint Nextel] also expressed willingness to limit our recommended CLEC certification proposal to CLECs that base their rates either on the rural benchmark or the rural exemption.").

[89] *See generally Establishing Just and Reasonable Rates for Local Exchange Carriers*, Comments of Hypercube, LLC and McLeodUSA Telecommunications Services, Inc. WC Docket No. 07-135 (filed Dec. 17, 2007); *see also Ex Parte* Letter from Tamar E. Finn, Counsel to PAETEC, to Marlene H. Dortch, Secretary, FCC, Docket No. 07-135 (filed Oct. 8, 2008); PAETEC June 12, 2008 *Ex Parte*; *Ex Parte* Letter from Tamar E. Finn, Counsel to Hypercube, LLC, to Marlene H. Dortch, Secretary, FCC, Docket No. 07-135 (filed May 14, 2008) (see also corresponding *ex parte* letter filed on May 16, 2008); *Ex Parte* Letter from Tamar E. Finn, Counsel to Pac-West Telecomm, Inc., to Marlene H. Dortch, Secretary, FCC, Docket No. 07-135 (filed April 23, 2008); *Ex Parte* Letter from Tamar E. Finn, Counsel to PAETEC, to

2. Revenue Sharing *Per Se* is Harmless and Pro-Competitive

"Revenue sharing" is a common business practice in the telecommunications market (including, but not limited to, by IXCs and marketing agents, international carriers, payphone providers and premises owners, operator service providers and traffic aggregators, and others), which the Commission has upheld numerous times against challenge. In fact, every discount off standard pricing offered by a communications provider to an end user is, in effect, a form of "revenue sharing" to that end user for stimulating traffic growth.[90]

Because CLECs rates are capped at the same rate level as the competing ILEC, access charge revenue sharing that creates an incentive for a customer to move from one LEC to another within the same territory is harmless to IXCs and end users, and a legitimate means of promoting competition between LECs. Access charge revenue sharing alone is therefore not the root cause of the traffic stimulation problem the Commission is seeking to address. That problem only arises under circumstances where revenue sharing becomes an incentive for portable, high-volume customers to locate in areas with extraordinarily high access charge rates based directly or indirectly on assumed higher costs and lower volumes. Any solution adopted by the Commission should target only the problem scenario and not revenue sharing in general.[91]

V. CONCLUSION

The Joint Commenters appreciate the Commission's efforts to reform intercarrier compensation and universal service. However, as described above, a number of the proposed reforms run the risk of being vacated upon judicial review, or could otherwise have significant unintended consequences to the telecommunications industry if put into practice. Thus, the Joint

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Marlene H. Dortch, Secretary, FCC, Docket No. 07-135 (filed April 15, 2008) (see also corresponding *ex parte* letter filed on May 2, 2008).

[90] *See* PAETEC June 12, 2008 *Ex Parte*, at 2.

[91] *See id.*

Commenters respectfully urge the Commission to modify its proposed reforms as set forth herein.

Respectfully submitted,

/s/

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Counsel for the Joint Commenters

Dated: November 26, 2008

Attachment A

Declaration of William A. Haas

REDACTED VERSION

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
High-Cost Universal Service Support	)	WC Docket No. 05-337
Federal-State Joint Board on Universal Service	)	CC Docket No. 96-45
Lifeline and Link Up	)	WC Docket No. 03-109
Universal Service Contribution Methodology	)	WC Docket No. 06-122
Numbering Resource Optimization	)	CC Docket No. 99-200
Implementation of the Local Competition Provisions in the Telecommunications Act of 1996	)	CC Docket No. 96-98
Developing a Unified Intercarrier Compensation Regime	)	CC Docket No. 01-92
Intercarrier Compensation for ISP-Bound Traffic	)	CC Docket No. 99-68
IP-Enabled Services	)	WC Docket No. 04-36

November 26, 2008

DECLARATION OF WILLIAM A. HAAS

I, William A. Haas, on oath, state and depose as follows:

I. INTRODUCTION

1. My name is William A. Haas. I currently serve as Vice President - Regulatory and Public Policy of PAETEC. PAETEC has three primary operating subsidiaries – PAETEC Communications, Inc., US LEC, and McLeodUSA Telecommunications Services, Inc. that all do business under the PAETEC name (hereinafter jointly referred to as "PAETEC"). I am submitting this

Declaration to provide a factual basis for the comments and recommendations PAETEC submits on several issues related to the inter-carrier compensation and Universal Service Fund ("USF") proposals currently being considered by the Federal Communications Commission ("FCC") in the above-referenced dockets, including an estimate of the true number of hours it takes PAETEC to fill out Form 499-A, the estimated amount of time PAETEC will require to create, modify and test its internal reporting systems to comply with any new or revised USF reporting requirements, PAETEC's average customer contract length, state commission prohibitions on CLECs inclusion of "change of law" provisions in customer contracts, and other related information.

II. BACKGROUND

2. After graduating from law school in 1982, I began working for the Iowa State Commerce Commission as an Administrative Law Judge. In July 1983, the Iowa State Commerce Commission was restructured, and I became an Assistant General Counsel in the newly created Office of General Counsel, legal advisor to the re-named Iowa Utilities Board. In October 1984, I joined the Iowa Office of Consumer Advocate as an Assistant General Counsel working on electric, gas and telecommunications rate cases and other matters that came before the Iowa Utilities Board. In 1995, I accepted a position as an Assistant General Counsel with McLeod Telemanagement, Inc., which, in 1996, became McLeodUSA Incorporated, parent company of McLeodUSA Telecommunications Services, Inc., a certificated competitive local exchange carrier.

3. At McLeodUSA, I was initially responsible for state regulatory matters and providing legal support for vendor relations, including relations with the Regional Bell Operating Companies, and the Sales and Marketing organizations. In 2003, I became responsible for all regulatory compliance and public policy matters, as well as providing legal support to the Marketing, Sales and Finance organizations. I was promoted to Deputy General Counsel in 2005. In 2008, McLeodUSA was acquired by PAETEC. My primary responsibilities at PAETEC include federal and state public policy advocacy, regulatory compliance and vendor relations legal support.

III. PAETEC'S FACTUAL INFORMATION

4. On average, it takes PAETEC approximately 20 hours to compile and complete the Forms 499-As for each of the various operating companies that are filed with the Universal Service Administrative Company ("USAC") each year. Each quarter a staff of four people in the Regulatory organization are required to coordinate with members of the Finance, Marketing and IT departments to gather the data required to complete the Form 499A forms. In addition, the Regulatory team has to coordinate with the Sales and IT organizations to record and monitor USF exemption information gathered from wholesale and retail customers. The workload is significantly greater in the 2nd quarter of each year.

5. The bulk of PAETEC revenue is generated by providing telecommunications services to business customers under written service agreements. These agreements can have term lengths up to five years. The average end user

service agreement for the McLeodUSA customer base has a term length of greater than four years. The average end user service agreement for the PAETEC Communications, Inc. customer base is around three years. On a combined basis, the average end user agreement term length for all PAETEC business customers is just under four years. Certain state utility commissions in which PAETEC operating companies have large customer bases have in the past (and in some instances to this day) prohibited PAETEC operating companies from including unencumbered "change of law" provisions in end user contracts. State commissions in Minnesota, Colorado and Ohio prohibited use of standard service agreement templates that included unencumbered change of law provisions that would enable PAETEC to unilaterally modify terms and conditions in response to regulatory changes.

6. In 2002, PAETEC's McLeodUSA operating subsidiary modified its pricing structure to incorporate all separate line charges into the base rate in an effort to offer simplified bundled pricing. The subscriber line charge was eliminated as a separate charge. As a result, McLeodUSA modified its tariffs and standard service agreement for its Preferred Advantage products to expressly provide that Subscriber Line and End User Common Line Charges ("SLCs") would not be a separate line item charges. McLeodUSA, therefore, would not be able to adjust its retail pricing to recoup lost intercarrier compensation revenues through increased SLC charges absent action by the Commission to ensure that McLeodUSA could unilaterally modify its contracts without

permitting customers from terminate their respective agreements in response to implementing SLCs.

7. The decrease from intrastate to interstate access rates would have a substantial revenue impact on PAETEC. For example, reducing current intrastate access rates to interstate access rate levels would cause a ***REDACTED***% decline in access revenues. If the rate is further decreased to $ .002, PAETEC will experience a ***REDACTED*** decrease when access rates (unified at the interstate level) are reduced to $0.002.

CHANGE FROM INTRA- TO INTERSTATE RATE	
Decrease in Revenues	***REDACTED***

CHANGE FROM CURRENT TO $.0007	
Decrease in Revenues	***REDACTED***

CHANGE FROM INTERSTATE RATES TO $.0007	
Decrease in Revenues	***REDACTED***

CHANGE FROM INTERSTATE RATES TO $.002	
Decrease in Revenues	***REDACTED***

8. PAETEC has filed forward looking TELRIC cost studies to support terminating access rates that exceed the ILEC's intrastate rates in the following states: Illinois, Texas, Colorado, New York, Minnesota, Ohio, Missouri and South Dakota. PAETEC has used these TELRIC costs studies to justify cost-based terminating intrastate access rates that are higher than the intrastate rates of the ILEC's. As explained by Mr. Starkey, however, PAETEC's cost of termination does not vary based on the type of traffic (local, intrastate long distance, VoIP, or interstate long distance) terminated by PAETEC.

IV. DECLARATION

9. I declare that I created this Declaration with the assistance of persons under my direct supervision and that, to the best of my knowledge, the facts represented herein are true and accurate.

William Haas

Attachment B

Declaration of Joseph O. Kahl

REDACTED VERSION

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	
High-Cost Universal Service Support	WC Docket No. 05-337
Federal-State Joint Board on Universal Service	CC Docket No. 96-45
Lifeline and Link Up	WC Docket No. 03-109
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Developing a Unified Intercarrier Compensation Regime	CC Docket No. 01-92
Intercarrier Compensation for ISP-Bound Traffic	CC Docket No. 99-68
IP-Enabled Services	WC Docket No. 04-36

November 26, 2008

DECLARATION OF JOSEPH O. KAHL

I, Joseph O. Kahl, on oath, state and depose as follows:

I. INTRODUCTION

1. My name is Joseph O. Kahl. My business address is 196 Van Buren Street, Herndon, Virginia 20107. I am Senior Director, Regulatory and External Affairs of RCN Corporation, parent of RCN Telecom Services, Inc. (“RCN”).

2. I am submitting this Declaration to provide a factual basis for the comments and recommendations RCN submits on several issues related to the inter-

carrier compensation and Universal Service Fund ("USF") proposals currently being considered by the Federal Communications Commission ("FCC") in the above-referenced dockets, including RCN's average customer contract length, and estimates on the effect of the Commission's intercarrier compensation proposals on the Company's revenues.

II. BACKGROUND

3. I joined RCN Corporation in April 1997. I am responsible for the regulatory oversight of commission dockets and other regulatory matters, as well as for maintaining certifications and compliance in the states where the company does business, and for the company's interconnection negotiations. I have over 20 years of experience in the telecommunications industry.

4. I graduated from Rutgers University in 1979 with a Bachelors degree in Accounting and Economics. I worked for Prudential-Bache Securities, Inc., from August 1979, to July 1982 as an accountant. I have been involved in a variety of management positions in the telecommunications field for over fifteen years. From July 1982, to December, 1993, I worked at LDDS/Metromedia Communications, first as Supervisor, Budgets and Inventory Control, then as Manager, Line Cost Analysis, and finally as Manager, Regulatory Affairs. From December 1993 through March 1997, I worked for MFS Communications Company and then for WorldCom. At MFS, I held the position of Director, Regulatory Affairs. I was responsible for federal and state tariffs for all company operating subsidiaries, ensuring regulatory compliance with state and federal rules, interexchange certification

initiatives in all fifty (50) states, interconnection and resale negotiations with Bell Atlantic, and developing and implementing regulatory policies on both state and federal levels.

III. RCN's FACTUAL INFORMATION

5. The average length of RCN's customer contract is over ***REDACTED*** months. However, certain RCN subsidiaries offer contract terms of ***REDACTED***.

6. RCN estimates that reducing switched access rates to $.0007 per minute of use ("MOU") would result in a reduction of approximately ***REDACTED*** in RCN's switched access revenues. This estimate is based on RCN's actual July 2008 revenues compared to what those revenues would have been under a $.0007 MOU rate.

IV. DECLARATION

7. I declare that I created this Declaration with the assistance of persons under my direction and that, to the best of my knowledge, the facts represented herein are true and accurate.

Joseph O. Kahl